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SUBJECT: SOUTH KOREA ECONOMIC BRIEFING - JANUARY 2010

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Domestic Economy

12. (SBU) Korean Economy Achieves Positive Growth in 2009:
The South Korean economy grew at a slower pace in the final quarter of 2009, but recorded growth 6.0 percent higher growth than in the disastrous fourth quarter of 2008. The ROK economy finished 2009 with positive growth of .2 percent, a remarkable achievement in the midst of the global financial crisis. Government expenditures and net exports of goods and services made up for the sluggish investment and private consumption throughout the year. Many economists expect up to five percent growth in 2010.

13. (SBU) Finance Minister Rules Out Quick Exit Policy Strategy:
Finance Minister Yoon Jeung-hyun told reporters on January 18 that Korea would not yet implement an exit strategy because the withdrawal of extraordinary fiscal and monetary policies will negatively affect the ongoing economic rebound. The Korean economy has rebounded more quickly than most developed economies. Both Minister Yoon and President Lee Myung-bak have stressed the need for job creation in the private sector. Given these factors, Yoon emphasized that it is too early to abandon the government's expansionary policies.

14. (SBU) Central Bank Keeps Record Low Interest Rates: The Bank of Korea (BOK)'s Monetary Policy Committee announced on January 8 its decision to keep the benchmark interest rate on hold at an annual 2.0 percent over the next five weeks. The interest rate has been constant for eleven consecutive months since falling 50 points in February 2009. Analysts have concluded that the central bank's postponement of the rate hike reflects mixed economic signals and political pressure to slow interest increase. In a break from

customary practice, after the BOK Governor indicated a possible hike in interest rates, the Finance Ministry sent Vice Minister Hur Kyung-wook to attend the January Monetary Policy Committee session.

15. (SBU) Consumer Prices Show Modest Inflation; Producer Prices Down: According to the National Statistics Office, the consumer price index averaged an annual 112.8 in 2009, up 2.8 percent from 110.0 in 2008. Prices for oil products fell from a year ago, but services, industrial and agriculture products led the overall price rise. The producer price index for 2009 stood at 110.9, down .2 percent from the previous year. Trade Surplus Hits Record High in 2009 The Korea Customs Service (KCS) reported on January 13 that exports and imports in 2009 totaled USD 363.5 billion and USD 323.1 billion, respectively, resulting in a USD 40.4 billion surplus. The annual trade surplus was a record high, surpassing the previous record of USD 39 billion in 1998. The surplus is more reflective of an extreme contraction of imports (-25.8 percent) compared with exports (-13.9 percent).

16. (SBU) MOSF Projects GNI to Reach USD 22,000 to 23,000 in 2010: The Ministry of Strategy Finance (MOSF) said on January 14 that, in the wake of the global recession, South Korea's nominal gross national income (GNI) per capita stood at about USD 17,000 in 2009, down to the level of four years ago. The GNI figure was based on 0.2 percent in GDP growth and an annual average won-dollar exchange rate of 1,276 in 2009. The government projected GNI per capita to reach USD 22,000 to 23,000 in 2010 and a won-dollar rate average of 1,100 to 1,150.

17. (SBU) Chaebols Plan Domestic Investments of USD 77 Billion in 2010: At a meeting of 30 major conglomerates on January 15, the Federation of Korean Industries (FKI) revealed that companies plan to invest 87 trillion won (USD 77 billion) in the ROK in 2010, up 16.3 percent from 2009 (74.8 trillion won or USD 58.6 billion). The companies anticipate hiring 79,199 people the year, or 8.7 percent more than they did in 2009, the FKI added.

18. (SBU) Report: Over 4 Million Jobless in ROK: The Korea Times on January 20 reported that over 4 million people are jobless, the highest figure since 2003. According to government statistics, the unemployment rate was 3.6 percent in December, rising by only 0.4 percentage points from the previous year. Unemployment reached 4.1 million, including jobless full-time workers (889,000) and people working less than 18 hours a week (960,000), people studying or training for jobs (590,000), and 1.5 million persons not seeking work. Government unemployment statistics only account for the 3.2 million people who are not looking for jobs. Economists point out the problem with the job market is systemic, not temporary and fewer people will get jobs despite the economic recovery. According to the Korea Listed Companies Association, the top 10 conglomerates employed 445,159 people as of the third quarter last year, up a mere 0.77 percent from the end of 2008. Employment even decreased in four of the top ten conglomerates.

19. (SBU) NTS to Increase Number of Audits: The nation's tax agency will increase the number of tax inspections back to the pre-financial crisis level, 18,500 tax audits, Baek Yong-ho, Commissioner of the National Tax Service (NTS). The planned inspections will likely focus on value-added taxes and capital gains taxes. The NTS scaled back its tax audits after the global crisis to 14,838 in 2008 and maintained the same rate in 2009, though the exact number has not been released. The tax office launched a 15-member taskforce, the "Overseas Tax Evasion Report Center," in November to crack down on offshore tax evaders and monitor illegal capital outflow.

20. (SBU) FX Reserves Slip in December; Tally Record Growth for 2009: The BOK announced that foreign currency reserves stood at USD 269.99 billion at the end of December 2009, decreasing USD 900 million from November and marking the first monthly drop in ten months. The fall was due to the weakening euro and yen. On an annual basis, however, foreign reserves grew by a record USD 68.77 billion.

21. (SBU) HSBC: Korean Economy to Grow 5.2 Percent in 2010: According to a report released December 23 by the Hong Kong and Shanghai Banking Corporation Limited Seoul Securities Branch (HSBC

Seoul Securities Branch), Korea's GDP growth for 2010 is forecast to be 5.2 percent and 4.8 percent in 2011. HSBC Seoul expected the BOK to raise the benchmark interest rate by 50 points in the first quarter of 2010. The report predicted the current account surplus-to-GDP ratio of 5.1 percent in 2009 to drop to 2.6 percent in 2010 and further to 1.9 percent in 2011. HSBC predicted the won-dollar exchange rate will average 1,113 in 2010 and 1,050 in 2011.

¶12. (SBU) Universal Studios to Open Theme Park in South Korea: Universal Studios signed an agreement with a South Korean consortium to build Asia's largest theme park about 60 kilometers southwest of Seoul. According to the Korea Times on January 19, the USD 2.67 billion deal joining Universal Parks and Resorts and 14 local partners, including POSCO E&C, Korea Water Resources Corporation and Lotte Group, revived an earlier plan that had been delayed for two years due to the global financial crisis. Developers expect to attract 15 million visitors annually to the giant theme park designed to be bigger than Universal Studios' four other theme parks combined.

¶13. (SBU) Development Assistance Fund to Increase Over 50 Percent: MOSF said in a January 10 press release the ROKG would increase the Economic Development Cooperation Fund (EDCF) 51.6 percent from the previous year to USD 470 billion in 2010. In particular, large projects totaling over USD 50 million will have greater support than those in the USD 20-30 million range so as to provide practical help to developing countries and support Korean companies' entry into overseas markets.

Finance and Structural Policies

¶14. (SBU) Kumho Restructuring Plan Falters: The creditor-led restructuring of the cash-strapped Kumho Asiana Group is getting off on the wrong foot, with disputes growing between the group, creditors and other stakeholders over how to resolve the option deal Kumho signed with financial investors when taking over Daewoo Engineering & Construction in 2006. Creditors are insisting that investors should sustain the losses by taking responsibility for their investment decisions. On January 22, the JoongAng Daily reported financial investors proposed a new plan to revive Kumho Industrial, which was put under a debt workout program by the creditors. Under the new plan, the financial investors will buy a 50 percent stake plus one share in Kumho Industrial for 2.2 trillion won (USD 1.9 billion) to be funded by local and foreign banks and local pension funds. But, on January 23, the Maeil Business Newspaper also reported that the Korea Development Bank, the main creditor, refused the proposal, as unrealistic. Local media attribute problems in the debt repayment programs to disputes among founding family members and creditors about how to restructure the group.

STEPHENS